

**Gulfsands Petroleum – Reporting Monday, 4 April**

Gulfsands Petroleum is an oil and gas exploration company with operations concentrated in the MENA region. Their primary exploration sites are in Syria and Tunisia. They also have production facilities in Syria with plans for further expansion. In the US, they have interests in the Gulf of Mexico with proven and probable reserves of 3.4 million barrels of oil equivalent (Mmboe).

**Fundamental view**
**Bull points:**

- Renewal of Kerkouane (offshore Tunisia) exploration licence for another three years
- The company has no debt and a healthy cash position in excess of \$80 million
- Good working relationship with the Syrian government

**Bear points:**

- Twaiba 1 site is no longer expected to find commercial quantities of oil or gas and drilling has been suspended for the time being
- The potential for political unrest to escalate in the MENA region may see investors shy away from the stock

**Management outlook, developments and market expectations - what should you look out for?**

Gulfsands Petroleum recently suspended drilling at the Twaiba 1 site in Syria as only high salinity water was found at the location. The company will determine the source of the salinity water and whether it is preventing the flow of hydrocarbons to the surface but CEO Ric Malcolm commented that a commercial result is unlikely. This was a blow to the company and explains some of the weakness in the stock's performance in recent months.

The company has a 50% interest in two other exploration wells in Syria: Abu Ghazal 1 and KHE-101. Evaluation and testing at these wells are expected to be completed by the end of April. Investors will want an update on the other exploration wells planned in Syria for 2011.

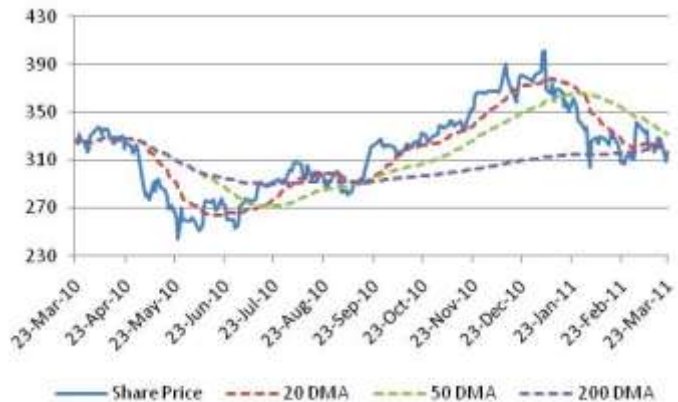
They have two early production facilities (EPFs) in Syria; Khurbet East with a capacity of 18,000 bopd and Yousefieh with a 3000 bopd capacity. The production from these facilities is the main source of cash for the business. They are planning to create a central processing facility (CPF) at Khurbet East by 2012 with a capacity of 50,000 bopd.

In Tunisia, the last update on the Sidi Dhafer well indicated that drilling was expected to begin in the second half of February. The Tunisian government also recently extended the Kerkouane exploration licence for a further three years. Gulfsands Petroleum has a 30% stake in this venture, with ADX Energy the main operator.

The Gulf of Mexico business is expected to be divested in 2011 as the company sees the asset base as mature with limited further upside.

**Key technicals**

The stock has lost 16.63% since the start of the year and has been hovering near 320p since February. Shares are trading below the 200-day moving average and have failed to break above the 50-day moving average since mid-January, a bearish trend which could continue if the situation in MENA deteriorates. Interestingly, the stock has been finding a lot of support near 310p, or close to a market capitalisation close of £380 million, which is the amount that Indian Oil Corp offered for the company in March 2010. This may provide a psychological floor to the stock price going forward.

**Gulfsands Petroleum - 12-month share price performance**


Source: Bloomberg

**At a glance**

Reporting date & time	Monday, 4 April @ 7:00am (London time)
Period	Full year results, ending 31 Dec
Company	Gulfsands Petroleum PLC
Ticker	GPX:LN
Industry/sector	Energy
Main index constituent	AIM All Share
Market Capitalisation (as at close 23 Mar)	386,430,900
Share price (as at close 23 Mar)	317
52 week high	411
52 week low	239
Volume (as at close 23 Mar)	292,842
Average 6m volume	471,691.30
Beta / Sector Beta (as at close 23 Mar)	0.70 / 0.90
Altman Z-score	8.49

Key Financials	Expectations	FY (31 Dec)	Change
	Thousands (\$)	Thousands (\$)	% (y-o-y)
Revenue	120.93	84.42	57.49%
Gross profit margin	-	55.03	6.13%
Operating profit margin	44.10	33.25	37.25%
Income before extraordinary items	52.78	27.83	-
Diluted EPS exc. one off items	0.44	0.23	-
Dividend per share	0	0	-

**Fundamental Ratios and Valuation**

Multiples	Forward	Historic	Sector
Return on common equity (ROE)	32.68	22.44	-10.18
Debt to equity (DE)	-	0.00	24.65
Dividend yield	0.00	0.00	0.18
Payout ratio	0.00	0.00	6.38
Price to earnings multiple (PE)	7.75	14.44	-
Price to sales ratio (PS)	5.19	5.75	4.53
Price to cashflow (PCF)	12.44	9.77	1099.25
Enterprise Value / EBITDA	4.27	6.55	-
Price to book multiple (PB)	3.25	3.85	2.34
Price to tangible book multiple (PTB)	-	4.32	-

Number of analysts covering stock	11
Number of Buy/ Hold/ Sell Recommendations	7/ 4/ 0
Median price target	420
Potential upside/downside (as at close 23 Mar)	32.49%

Source: Bloomberg

# BASIC DEFINITIONS

(Alphabetically sorted)

## DEFINITION

**Altman's Z-score** is used to predict the probability that a company will go bankrupt within two years. The model uses a combination of five different financial ratios to approximate the chance of bankruptcy. Generally speaking, the lower the score the more likely a company will go bankrupt, with scores above 3 considered healthy, and scores between 1.8 and 3 in the grey area. The score was traditionally designed for manufacturing companies with assets over \$1 million and is not suitable for use with financial companies which tend to have complex balance sheets.

**Average return on equity** is the amount of net income earned per unit of equity ownership. It is calculated by dividing net income by the average of beginning shareholders' equity and ending shareholders equity. The measure gives an indication of the company's efficiency in deriving returns on the amount of equity the company holds.

**Beta** is a measure of systematic risk, or the risk that cannot be removed through diversification. Beta gives an indication of the sensitivity of a stock to movements in the market. A beta of 1 indicates the stock will move in line with the market, a beta less than 1 means the company is expected to be less sensitive to changes in the market, while a company with beta greater than 1 may see more volatile share price movements compared to the market.

**Dividend per share** is the proportion of profits paid out to each common stock shareholder. The figure is derived by dividing the dividend by the number of shares outstanding or by multiplying the payout ratio by the total net income and dividing that by the number of shares outstanding to common stock shareholders

**Dividend yield** reveals how much a company pays out in dividends each year relative to the current share price. It is derived by dividing the latest full year dividend per share by a company's price per share. Income investors will prefer companies that have higher dividend yields. On the other hand, this metric would not be significant for the growth investor because companies focusing on aggressive growth will reinvest the majority of dividends.

**Earnings Before Interest, Tax, Depreciation & Amortisation (EBITDA)** is a measure of cash earnings generated a company's core operations. Although similar to operating profit, it differs in that it eliminates certain items that are treated differently under foreign accounting principles – interest, tax, amortisation and depreciation. As a result an investor is able to compare like with like when assessing the operating profits of peer companies across various jurisdictions.

**Earnings per share (EPS)** are calculated by dividing net income by the number of shares outstanding, although a more advanced option is to use the weighted average number of shares outstanding. Another version of the EPS is known as diluted EPS, which is used as a gauge for measuring the quality of a company's earnings if all convertible securities were exercised; convertible preferred shares, convertible bonds, stock options and warrants are examples of convertible securities.

**Enterprise value to EBITDA (EV/EBITDA)** is sometimes used as an alternative to the PE ratio. Its advantage over the PE ratio is that it is not affected by a company's capital structure, which is affected by the amount of debt a company holds. In this respect, EV/EBITDA can make cross-company comparisons more meaningful. Enterprise Value (EV) reflects the market value of the business and is calculated by taking the market capitalisation of a company and adding back the market value of the company's debt and preferred shares, while deducting minority interests and cash.

**Gross margin** represents the amount of gross income generated for a given amount of sales, expressed in percentage terms. A higher ratio means that a company is able to turn materials into a finished product in a more efficient manner.

**Market capitalisation** represents the total market value of the company. It is derived by multiplying the total number of shares outstanding by the current price per share.

**Net debt to equity ratio** reflects a company's capital structure, indicating the proportion of debt the company is using to finance assets. Net debt is calculated by combining short term and long term borrowings, and taking away cash and cash equivalents.

If too much debt is used to finance operations, the company could potentially generate more earnings, but would increase earnings at a higher risk. The cost of debt financing may outweigh the return that the company generates on the debt and lead to bankruptcy. Generally, a low debt to equity ratio is preferred, but this should be compared to the sector. Capital intensive industries such as auto manufacturing tend to have high debt/equity ratios above 2 while personal computer companies have a lower ratio.

**Payout ratio** measures the percentage of net income that is used to pay dividends to shareholders. A higher payout ratio would benefit investors seeking higher current income, whereas a low payout ratio may imply that the company is paying less in dividends in order to reinvest the earnings on further growth opportunities.

**Price to book ratio (PB)** reflects the premium or discount that investors place on a company's net worth or, put another way, an indication of how much shareholders are paying for the net assets of a company. Investors would be willing to pay a premium over a company's net asset value only if they believe that the company is robust, growing rapidly and generating high returns on equity. It is derived by dividing a company's share price by its shareholders' equity. A high P/B ratio may mean that a company is over-valued. In the US assets in the balance sheet are recorded at historical cost but outside of the US some countries allow for the revaluation of property, plant and equipment which increases the validity of the measure.

**Price to earnings growth ratio (PEG)** is a measure of a company's value taking into consideration the growth in earnings. It is measured by dividing the PE ratio by the earnings growth rate. As a general guide, when the PE ratio equals its growth rate the PEG ratio would equal 1, suggesting that the company is fairly priced.

**Price to earnings ratio (PE)** is derived by dividing the current price of a company with its latest annual earnings per share. A high ratio may mean that a company is over-valued but at the same time could reflect investors' willingness to pay a premium on every dollar of earnings. The premium could be justified if the investor believes that the company will grow at a faster pace than the market expects. Growth companies generally have a high PE because investors expect higher earnings growth.

**Price to tangible book value (PTB)** Is similar to PB except it removes a company's intangible assets (including goodwill) from the shareholders' equity figure in the balance sheet. Intangible assets are removed because they are prone to valuation issues and are hard to sell in the case of bankruptcy.

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